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CENTRAL INTELLIGENCE AGENCY

OFFICE OF NATIONAL ESTIMATES

*Formerly
staff memo 24-72*

21 July 1972

MEMORANDUM

SUBJECT: The IPC Case: As Controversial as Ever*

NOTE

The recent estimate on Peru (NIE 97-72, 13 April 1972) indicated that US-Peruvian relations had become less abrasive, as compared with 1968-1969, in part because the IPC case had been shunted to the sidelines. The estimate further indicated that the issue was not settled and could come back to haunt officials in both countries. In fact, secret negotiations on a compromise IPC settlement were underway as we wrote. These have since been broken off, under circumstances that have indeed contributed to a new wave of tensions in US-Peruvian relations. This paper reviews the history and current status of the IPC issue.

* This memorandum was prepared by the Office of National Estimates and coordinated within CIA.

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1. After two years of gradual improvement, relations between the US and Peru have begun to deteriorate again. The case of the expropriated International Petroleum Company (IPC)-- apparently shunted to the sidelines for a while by both governments -- has come back to haunt officials in Washington and Lima. Secret negotiations aimed at resolving the impasse collapsed because of press leaks in Peru. The Peruvian Government reacted by going through the final formalities, which they delayed doing for four years, to expropriate the IPC, and by publicly berating the US for its long-standing policy of blocking credits to Peru from multinational lending circles. The visits of former Treasury Secretary Connally and Federal Reserve Chairman Arthur Burns have not, to the best of our knowledge, led to any change in the Peruvian position.

2. Spokesmen for the Peruvian military reacted shrilly, and we believe predictably, to the exposure of the talks because the IPC case remains the single most emotionally charged issue in Peruvian domestic politics, as it has been much of the time over the last 60 years. The government could not be seen in public as compromising on this issue, for the popular uproar would jeopardize its political position and cast doubts on its credibility as a revolutionary force. The IPC has always been an exceptional case, and the current brouhaha simply underlines its continued importance.

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A Bit of History

3. In 1889, the London and Pacific Petroleum Company came into possession of the oil-rich La Brea-Pariñas region near the northern coastal settlement of Talara, Peru. For a modest sum, the British businessmen bought from the Peruvian Government sub-soil exploration rights for ten *partenencias* of land. The Peruvian Government thought it was selling approximately 100 acres. It was not until 1914, however, that the Peruvian authorities finally got around to measuring and surveying this land. It was discovered at this time that London and Pacific was actually utilizing 41,614 *partenencias* (416,140 acres).

4. Naturally this caused a great public furor. Many congressional leaders and a leading newspaper publisher insisted that the British company should be forced to pay back taxes and then be driven from the country. Instead, the Peruvian congress agreed to submit the dispute to an international tribunal, meeting in Paris, which chose in 1921 to confirm the questionable claim of the company and to give it a special tax status for another 50 years. Peruvian nationalists were furious, and the arbitration decision was never ratified by the Peruvian congress. London and Pacific discreetly sold its concessions to the IPC,

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which is incorporated as a Canadian concern but is in fact a fully owned subsidiary of the Standard Oil Company of New Jersey.

5. The IPC case remained a burning political issue throughout the 1920s. A special Peruvian commission ruled the Paris decision invalid, but the matter was dropped because of various political pressures. In 1946, however, the company was back in the headlines. The government in power at the time, hard pressed by economic problems, gave IPC the right to explore for new deposits on land that had been set aside as a national reserve. Several congressmen, business leaders, and newspapers complained of a "sell-out", and the ensuing ruckus led to the assassination of one editor.

6. Still another effort to settle the conflict over IPC's various concessions was made in 1960, but vitriolic speeches by Peruvian nationalists about "capitalistic exploitation" forced the government to back down. Two years later, the ruling military government promised to resolve the case in line with nationalist demands, but it retreated in the face of warnings from the US Government and ultimately decided to let its civilian successor, President Belaunde, deal with the problem. Belaunde actually opened negotiations with the IPC early in his term, but the talks

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failed, in good measure because of the company's intransigence. The Peruvian congress then declared the Paris settlement of 1921 null and void.

7. As time went by, Peruvian nationalists called with increasing vehemence for expropriation of the IPC, while in the US the affair was played up as a test case for Peru's credit-worthiness. The US reduced its assistance to Peru and applied pressure on the government in various other ways. A compromise was eventually reached, in which the IPC acknowledged the ownership rights of the state to the ground beneath its oilfields and declared that it would turn its facilities over to the government. In exchange the government was to relinquish all claims to alleged tax debts and to grant the company the right to operate its refinery and to continue its trade monopoly for an additional 80 years. Regarded by nationalist circles as a betrayal of "national property", the agreement (known as the Act of Talara) was never carried out. Belaunde's government was overthrown by the military, on 3 October 1968, and they annulled the agreement the very next day.

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SECRET*The IPC Case under the Military Regime*

8. The highly nationalistic Peruvian armed forces felt strongly about the IPC, and they used the issue to create immediate popular support for their regime. President Velasco, who well understood the symbolic importance of the IPC, sent troops to occupy the oilfields and refinery. The government then announced that the company had been expropriated, proclaimed a "Day of National Dignity", and turned the question of compensation over to the courts. The IPC, backed up by the State Department, demanded \$120 million. The Peruvian courts set the figure at \$71 million, but the money was never paid because the regime demanded \$690 million from the IPC to cover past unpaid taxes and "illegal profits".

9. The relationship between the US and Peru entered what was perhaps the most strained phase in its history. The US acknowledged Peru's right to expropriate foreign property but insisted upon a negotiated settlement of the compensation question and, above all, on respect for international legal norms, which it felt had been violated by annulment of the Paris decision of 1921. Officials in Washington debated the usefulness of applying the Hickenlooper Amendment, which would have meant an end of US development aid and elimination by the US of Peru's sugar quota.

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10. The US never did apply the Hickenlooper Amendment to Peru, but it did cut back on most ongoing programs. The Irwin mission in 1969 attempted to work out a deal, but Velasco and his colleagues were unwilling to change their position. Indeed, the regime announced that the IPC issue was "resolved". The US decided to avoid a confrontation and eight months later was able to demonstrate good will by giving substantial assistance following a disastrous Peruvian earthquake. The US stopped its active efforts to discourage private credits and loans to Peru, although it maintained its refusal to sanction any official assistance by US or international lending agencies. Official relations improved gradually until the collapse of the recent negotiations.

11. We do not know what went on at the secret talks held in early 1972. The Peruvian Government, however, made it clear from the beginning that it could never admit to a deal publicly. Apparently, officials in Lima were willing to discuss the issue because they wanted the full support of the US in international lending circles, and the US insisted on some kind of IPC agreement first.

The Outlook

12. The Peruvian Government is in an awkward position. It wants and needs the good will of the US Government to further its

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programs of national transformation but cannot accede to US wishes on the IPC case without damaging its political position at home. Peru's major interest groups -- the students, the labor unions, businessmen, the APRA -- are increasingly unhappy with the government's performance generally. Most groups have been unwilling thus far to challenge actively the military's monopoly of political power. But the students have recently begun just such a challenge through street demonstrations.

13. Thus, the regime is not in a strong enough position to take an unpopular stand on IPC, even if it wanted to. The IPC affair is just too solidly implanted in the Peruvian psyche as an issue on which national dignity precludes compromise for this or any successor regime. Even if the regime has striking success with some of its revolutionary programs, its stance on IPC would change very slowly, at best. If US pressures on Peru are maintained, the Peruvians will probably become more intransigent and xenophobic in their relations with the US and less moderate and pragmatic in their approach to carrying forward the revolution. And there would probably be an increase in the influence of those Peruvians who seek confrontations with the US over such issues as Cuba, the law of the sea, arms purchases, the burgeoning US stake in new Peruvian oil finds, and US investment generally.

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MEMORANDUM FOR: Mr. Ray, C. G.
Director, CIA

Copies of the attached have been sent to
Dep. Assistant Secretary Graham, Mr. Byles,
Frechette and Sandy Pringle of HRM/LA.

JOHN HUIZENGA
Director
National Estimates

29 Aug 72
(DATE)

FORM NO. 101	REPLACES FORM 10-101	(47)
MEMORANDUM FOR: DCI		
I believe that I sent this to you before, but you may wish to know that one of Flanigan's people heard of it and requested it on his behalf. We are told that Flanigan, who had thought of IPC as the gents in the white hats, is now disposed to take a somewhat different view of the merits of that case.		
 John Huizenga		
<u>29 August 1972</u> (DATE)		
FORM NO. 101	REPLACES FORM 10-101 WHICH MAY BE USED.	(47)

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